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IOWA TRANSPARENCY NEWSLETTER

Iowa Needs to Bring Better Transparency to Pension Plans

by Jennifer L. Crull

Each year we update you on the Truth in Accounting "Financial State of the States," and each year we have to call out Iowa for not reporting the unfunded pension liability. Back in August it was reported in the *Iowa Transparency Newsletter* that Iowa only reports "$286 million in pension and retirees' healthcare benefits, yet owes $1.9 billion. Because the state government uses outdated accounting methods, a significant amount of liabilities are excluded from its financial reporting."[1] Why do we need transparency and truthfulness in our budgetary account? Here are the reasons laid out by Truth in Accounting:

- Lack of transparency leads to big problems
- Due to accounting tricks, balanced budget claims have given citizens a false sense of security, while states sink further into debt
- Citizens do not know the true cost of their state government, and taxes do not reflect the real cost of government
- Complex pension schemes (that citizens and even their elected officials cannot understand) have racked up state debt even further
- Voters have re-elected leaders based on claims that budgets were balanced
- Legislators have created new programs and increased services without knowing the true cost of current and future government spending
- Our representative form of government is being undermined because citizens have become cynical and mistrust their governments[2]

I am sure that we all can relate to one or more of the statements above, but there is hope! Over the last year there has been a significant change in how governmental bodies report pension liability, and this change will significantly improve

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transparency. The change is Governmental Accounting Standards Board (GASB) Statement Number 68, which is in effect for FY15. This change will "require states to report the full amount of their unfunded pension liabilities on the face of their balance sheets."[3] As you can read from the first paragraph, it will be a dramatic change for the state of Iowa, which has been reporting $286 million, but actually owes $1.9 billion.

So if you are wondering why these changes are so important, consider the following: "Pensions are a form of compensation, like salaries, which governments provide in return for work."[4] Therefore these liabilities need to be reflected on the balance sheet to have a true picture of government entities' true solvency. To put this in terms of our everyday life, let's suppose you have $150 in your checking account and you are deciding if you can afford to go out to eat when you know it will cost at least $40, but you didn't take into account you have a utility bill due in another week for $200. You haven't had to incur that expense yet, so you don't take it into consideration when making your decisions. Not the rules most of us get to live by.

The pension crisis is not a new phenomenon. This problem has existed for many years, and as the baby boomers are retiring this problem continues to grow as states continue to underfund their pension systems. Currently "10,000 baby boomers a day will reach retirement age."[5] That has a significant impact on retirement systems.

When it comes to retirement plans, we currently have two types: the defined benefit (DB) or defined contribution (DC). The DB, which is the type prevalent in most retirement plans, "places the risk of cost increases disproportionately on the government [taxpayers]," and DC model "limits current costs, but is largely self-directed and provides less reliable future guarantees for program participants."[6] While the DC model still has problems, the DB is the one that places the most strain on state governments.

For Iowa, most state employees are in the Iowa Public Employees' Retirement System (IPERS), which is a DB system. Currently the IPERS fund is only 84 percent funded, which means that the taxpayers have a liability for the remaining 16 percent. This information hasn't been reported before in

Summary of Pension Standards Changes	
Old Pension Standards	**New Pension Standards**
Unfunded pension liability hidden off-balance sheet	**Unfunded pension liability** will be reported on the face of government balance sheets
For multi-employer plans - each government's share of **unfunded pension liability** not calculated	For multi-employer plans - each government's share of **unfunded pension liability** will be calculated and reported on each employer's balance sheet
Unfunded pension liability called **"Unfunded Actuarial Accrued Liability" (UAAL)**	**Unfunded Pension Liability** called **"Net Pension Liability" (NPL)**
Plan assets called **"Actuarial Value of Assets" (AVA)**	Plan assets called **"Fiduciary Net Position" (FNP)**
Value of plan assets calculated using the **average market value** over 5 years	Value of plan assets calculated using **current market value**
Plan liability called **"Actuarial Accrued Liability" (AAL)**	Plan liability called **"Total Pension Liability" (TPL)**
Plan liability calculated using the historical rate of return	Plan liability calculated using the **"Blended Rate"**
"Annual Required Contribution": Calculation Required	**"Actuarially Determined Contribution":** Calculation Optional

Source: "New Pension Standard Brings Greater Pension Debt Transparency (Details)," Truth in Accounting, September 20, 2015, <http://www.truthinaccounting.org/news/detail/new-pension-standard-brings-greater-pension-debt-transparency-details>*, accessed February 12, 2016.*

a way that enables people to fully understand what IPERS has as liabilities. While Iowa currently is in a more solid place than many states concerning its retirement system, the state needs to think about the "under-funding in the future. The amounts owed to both current and future beneficiaries must be paid by future taxpayers – the younger workers of today and tomorrow. Unfortunately, many of these workers are already finding their financial future constrained."[7] That is why these changes are a huge move in increasing the transparency of how IPERS is really doing.

Employees of Public Interest Institute are available for speaking engagements on a variety of issues.

I hope that you can see how GASB 68 has helped to improve the transparency of pension funds in the United States and here in Iowa. Our economy can't afford a meltdown of the pension system, and for that reason it is important that governments have a true picture of what they owe to the retirees. We hope that IPERS will work to continue increasing the percentage that is fully funded over the next few years.

(Endnotes)

[1] "Iowa Hiding 85 Percent of Retirement Debt," Truth in Accounting, *Iowa Transparency Newsletter*, <http://www.iowatransparency.org/aug15newsletter.html>, accessed on

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[2] "Why is Truthful, Timely, and Transparent Financial Data Important?," Truth in Accounting, September 20, 2015, <http://www.truthinaccounting.org/news/detail/why-is-truthful-timely-and-transparent-financial-data-important>, accessed on February 11, 2016.

[3] "New Pension Standards Bring Greater Pension Debt Transparency," Truth in Accounting, September 20, 2015, <http://www.truthinaccounting.org/news/detail/new-pension-standard-brings-greater-pension-debt-transparency>, accessed on January 7, 2016.

[4] "Summary of Statement No. 68," Governmental Accounting Standards Board, June 2012, <http://www.gasb.org/jsp/GASB/Pronouncement_C/BSummaryPage&cid=1176160219492>, accessed on January 28, 2016.

[5] "Addressing the National Pension Crisis: It's Not a Math Problem," The PRM Group, 2013, p. 3, <https://www.pfm.com/uploadedFiles/Content/Knowledge_Center/Whitepapers,_Articles,_Commentary/Whitepapers/Addressing_the_National_Pension_Crisis_single_page.pdf>, accessed on February 12, 2016.

[6] Ibid.

[7] Deborah Thornton, "IPERS – Is 'OK' Good Enough?," Public Interest Institute, INSTITUTE BRIEF Vol. 21, No. 4, February 2014, < http://www.limitedgovernment.org/brief21-4.html>, accessed on March 2, 2016.

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